

104TH CONGRESS
1ST SESSION

S. 447

To provide tax incentives to encourage production of oil and gas within the United States, and for other purposes.

IN THE SENATE OF THE UNITED STATES

FEBRUARY 16 (legislative day, JANUARY 30), 1995

Mr. INHOFE (for himself and Mr. NICKLES) introduced the following bill;
which was read twice and referred to the Committee on Finance

A BILL

To provide tax incentives to encourage production of oil and gas within the United States, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE; TABLE OF CONTENTS.**

4 (a) **SHORT TITLE.**—This Act may be cited as the
5 “Domestic Oil and Gas Production Tax Incentive Act”.

6 (b) **AMENDMENT OF 1986 CODE.**—Except as other-
7 wise expressly provided, whenever in this title an amend-
8 ment or repeal is expressed in terms of an amendment
9 to, or repeal of, a section or other provision, the reference

1 shall be considered to be made to a section or other provi-
 2 sion of the Internal Revenue Code of 1986.

3 (c) TABLE OF CONTENTS.—The table of contents for
 4 this Act is as follows:

Sec. 1. Short title; amendment of 1986 code; table of contents.

TITLE I—PRODUCTION CREDIT

Sec. 101. Tax credit for marginal and new domestic oil and natural gas produc-
 tion.

TITLE II—MODIFICATIONS TO PERCENTAGE DEPLETION

Sec. 201. Elimination of net income limitation on percentage depletion for oil
 and gas.

Sec. 202. All marginal production eligible for percentage depletion.

Sec. 203. Allocation of depletable quantities.

Sec. 204. Percentage depletion rate for marginal production.

TITLE III—OTHER PROVISIONS

Sec. 301. Election to expense geological and geophysical expenditures.

Sec. 302. Enhanced oil recovery credit.

Sec. 303. Election for optional 5-year writeoff of intangible drilling costs.

Sec. 304. Allocation of deductions in determining net income.

5 **TITLE I—PRODUCTION CREDIT**

6 **SEC. 101. TAX CREDIT FOR MARGINAL AND NEW DOMESTIC** 7 **OIL AND NATURAL GAS PRODUCTION.**

8 (a) CREDIT FOR PRODUCING OIL AND GAS FROM
 9 NEW WELLS AND MARGINAL WELLS.—Subpart D of part
 10 IV of subchapter A of chapter 1 (relating to business cred-
 11 its) is amended by adding at the end the following new
 12 section:

1 **“SEC. 45C. CREDIT FOR PRODUCING OIL AND GAS FROM**
 2 **NEW WELLS AND MARGINAL WELLS.**

3 “(a) GENERAL RULE.—For purposes of section 38,
 4 the new and marginal well production credit for any tax-
 5 able year is an amount equal to the product of—

6 “(1) the credit amount, and

7 “(2) the qualified crude oil production and the
 8 qualified natural gas production which is attrib-
 9 utable to the taxpayer.

10 “(b) CREDIT AMOUNT.—For purposes of this sec-
 11 tion—

12 “(1) IN GENERAL.—The credit amount is—

13 “(A) \$3 per barrel of qualified crude oil
 14 production, and

15 “(B) 50 cents per 1,000 cubic feet of
 16 qualified natural gas production.

17 “(2) REDUCTION AS OIL AND GAS PRICES IN-
 18 CREASE.—

19 “(A) IN GENERAL.—The \$3 and 50 cents
 20 amounts under paragraph (1) shall each be re-
 21 duced (but not below zero) by an amount which
 22 bears the same ratio to such amount (deter-
 23 mined without regard to this paragraph) as—

24 “(i) the excess of the applicable ref-
 25 erence price over \$14 (\$2.49 for qualified
 26 natural gas production), bears to

1 “(ii) \$6 (\$1.06 for qualified natural
2 gas production).

3 The applicable reference price for a taxable
4 year is the reference price for the calendar year
5 preceding the calendar year in which the tax-
6 able year begins.

7 “(B) INFLATION ADJUSTMENT.—In the
8 case of any taxable year beginning in a calendar
9 year after 1995, each of the dollar amounts
10 contained in subparagraph (A) shall be in-
11 creased to an amount equal to such dollar
12 amount multiplied by the inflation adjustment
13 factor for such calendar year (determined under
14 section 43(b)(3)(B) by substituting ‘1994’ for
15 ‘1990’).

16 “(C) REFERENCE PRICE.—For purposes of
17 this paragraph, the term ‘reference price’
18 means, with respect to any calendar year—

19 “(i) in the case of qualified crude oil
20 production, the reference price determined
21 under section 29(d)(2)(C), and

22 “(ii) in the case of qualified natural
23 gas production, the Secretary’s estimate of
24 the annual average wellhead price per

1 1,000 cubic feet for all domestic natural
2 gas.

3 “(c) QUALIFIED CRUDE OIL AND NATURAL GAS
4 PRODUCTION.—For purposes of this section—

5 “(1) IN GENERAL.—The terms ‘qualified crude
6 oil production’ and ‘qualified natural gas production’
7 mean domestic crude oil or natural gas which is pro-
8 duced from—

9 “(A) a marginal well, or

10 “(B) a new well.

11 “(2) LIMITATION ON AMOUNT OF PRODUCTION
12 WHICH MAY QUALIFY.—

13 “(A) IN GENERAL.—Crude oil or natural
14 gas produced during any taxable year from any
15 well shall not be treated as qualified crude oil
16 production or qualified natural gas production
17 to the extent production from the well during
18 the taxable year exceeds—

19 “(i) in the case of a marginal well,
20 1,095 barrels or barrel equivalents, or

21 “(ii) in the case of a new well—

22 “(I) 5,475 barrels in the case of
23 crude oil, or

24 “(II) 109,500,000 cubic feet in
25 the case of natural gas.

1 “(B) SPECIAL RULE WHERE WELL PRO-
2 DUCES BOTH.—In the case of a new well which
3 produces crude oil and natural gas, the limita-
4 tion for any taxable year applicable to natural
5 gas produced from the well shall be reduced by
6 the barrel equivalents (expressed in cubic feet)
7 of the crude oil produced from the well during
8 the taxable year.

9 “(C) PROPORTIONATE REDUCTIONS.—

10 “(i) SHORT TAXABLE YEARS.—In the
11 case of a short taxable year, the limitations
12 under this paragraph shall be proportion-
13 ately reduced to reflect the ratio which the
14 number of days in the year bears to 365.

15 “(ii) WELLS NOT IN PRODUCTION EN-
16 TIRE YEAR.—In the case of a well which is
17 not capable of production during each day
18 of a taxable year, the limitations under
19 this paragraph applicable to the well shall
20 be proportionately reduced to reflect the
21 ratio which the number of days of produc-
22 tion bears to the total number of days in
23 the taxable year.

24 “(3) DEFINITIONS.—

1 “(A) MARGINAL WELL.—The term ‘mar-
2 ginal well’ means a domestic well (other than a
3 new well)—

4 “(i) which during the taxable year has
5 marginal production (as defined in section
6 613A(c)(6)), or

7 “(ii) which, during the taxable year—

8 “(I) has average daily production
9 of not more than 25 barrel equiva-
10 lents, and

11 “(II) produces water at a rate
12 not less than 95 percent of total well
13 effluent.

14 “(B) NEW WELL.—The term ‘new well’
15 means a domestic well drilled after December
16 31, 1994.

17 “(C) CRUDE OIL, ETC.—The terms ‘crude
18 oil’, ‘natural gas’, ‘domestic’, and ‘barrel’ have
19 the meanings given such terms by section
20 613A(e).

21 “(D) BARREL EQUIVALENT.—The term
22 ‘barrel equivalent’ means, with respect to natu-
23 ral gas, a conversion ratio of 6,000 cubic feet
24 of natural gas to 1 barrel of crude oil.

25 “(d) OTHER RULES.—

1 “(1) PRODUCTION ATTRIBUTABLE TO THE TAX-
2 PAYER.—In the case of a marginal well or new well
3 in which there is more than one owner of operating
4 interests in the well and the crude oil or natural gas
5 production exceeds the limitation under subsection
6 (c)(2), qualifying crude oil production or qualifying
7 natural gas production attributable to the taxpayer
8 shall be determined on the basis of the ratio which
9 taxpayer’s revenue interest in the production bears
10 to the aggregate of the revenue interests of all oper-
11 ating interest owners in the production.

12 “(2) OPERATING INTEREST REQUIRED.—Any
13 credit under this section may be claimed only on
14 production which is attributable to the holder of an
15 operating interest.

16 “(3) PRODUCTION FROM NONCONVENTIONAL
17 SOURCES EXCLUDED.—In the case of production
18 from a marginal well which is eligible for the credit
19 allowed under section 29 for the taxable year, no
20 credit shall be allowable under this section unless
21 the taxpayer elects not to claim the credit under sec-
22 tion 29 with respect to the well.”

23 (b) CREDIT TREATED AS BUSINESS CREDIT.—Sec-
24 tion 38(b) is amended by striking “plus” at the end of
25 paragraph (10), by striking the period at the end of para-

1 graph (11) and inserting “, plus”, and by adding at the
 2 end the following new paragraph:

3 “(12) the new and marginal oil and gas well
 4 production credit determined under section 45C(a).”

5 (c) CREDIT ALLOWED AGAINST REGULAR AND MINI-
 6 MUM TAX.—

7 (1) IN GENERAL.—Subsection (c) of section 38
 8 (relating to limitation based on amount of tax) is
 9 amended by redesignating paragraph (3) as para-
 10 graph (4) and by inserting after paragraph (2) the
 11 following new paragraph:

12 “(3) SPECIAL RULES FOR OIL AND GAS PRO-
 13 Duction CREDIT.—

14 “(A) IN GENERAL.—In the case of the oil
 15 and gas production credit—

16 “(i) this section and section 39 shall
 17 be applied separately with respect to the
 18 credit, and

19 “(ii) in applying paragraph (1) to the
 20 credit—

21 “(I) subparagraph (A) shall not
 22 apply, and

23 “(II) the limitation under para-
 24 graph (1) (as modified by subclause
 25 (I)) shall be reduced by the credit al-

1 lowed under subsection (a) for the
2 taxable year (other than the oil and
3 gas production credit).

4 “(B) OIL AND GAS PRODUCTION CRED-
5 IT.—For purposes of this subsection, the term
6 ‘oil and gas production credit’ means the credit
7 allowable under subsection (a) by reason of sec-
8 tion 45C(a).”

9 (2) CONFORMING AMENDMENT.—Subclause (II)
10 of section 38(c)(2)(A)(ii) is amended by inserting
11 “or the oil and gas production credit” after “em-
12 ployment credit”.

13 (d) COORDINATION WITH SECTION 29.—Section
14 29(a) is amended by striking “There” and inserting “At
15 the election of the taxpayer, there”.

16 (e) CLERICAL AMENDMENT.—The table of sections
17 for subpart D of part IV of subchapter A of chapter 1
18 is amended by adding at the end the following item:

 “45C. Credit for producing oil and gas from new wells and marginal wells.”

19 (f) EFFECTIVE DATE.—The amendments made by
20 this section shall apply to production after the date of the
21 enactment of this Act.

1 **TITLE II—MODIFICATIONS TO**
2 **PERCENTAGE DEPLETION**

3 **SEC. 201. ELIMINATION OF NET INCOME LIMITATION ON**
4 **PERCENTAGE DEPLETION FOR OIL AND GAS.**

5 (a) ELIMINATION.—

6 (1) IN GENERAL.—Paragraph (1) of subsection
7 (d) of section 613A (relating to the limitation based
8 on taxable income for percentage depletion in the
9 case of oil and gas wells) is repealed.

10 (2) OTHER PRODUCTION.—The second sentence
11 of subsection (a) of section 613 (relating to percent-
12 age depletion) is amended to read as follows: “Ex-
13 cept in the case of oil and gas wells, such allowance
14 shall not exceed 50 percent of the taxpayer’s taxable
15 income from the property (computed without allow-
16 ance for depletion).”

17 (b) EFFECTIVE DATE.—The amendments made by
18 this section shall apply to taxable years beginning after
19 December 31, 1994.

20 **SEC. 202. ALL MARGINAL PRODUCTION ELIGIBLE FOR PER-**
21 **CENTAGE DEPLETION.**

22 (a) IN GENERAL.—Paragraph (6) of section 613A(c)
23 (relating to marginal production) is amended to read as
24 follows:

1 “(6) SEPARATE APPLICATION TO MARGINAL
2 PRODUCTION.—

3 “(A) IN GENERAL.—Except as provided in
4 subsection (d)—

5 “(i) the allowance for depletion under
6 section 611 with respect to all of a tax-
7 payer’s marginal production of domestic
8 crude oil and domestic natural gas shall be
9 computed in accordance with section 613,
10 except that, for purposes of section 613(a),
11 the applicable percentage shall be sub-
12 stituted for the percentage specified in sec-
13 tion 613(b), and

14 “(ii) such marginal production shall
15 not be taken into account under paragraph
16 (1), including for purposes of determining
17 the taxpayer’s average daily production of
18 domestic crude oil or domestic natural gas
19 eligible for application of paragraph (1).

20 “(B) APPLICABLE PERCENTAGE.—For
21 purposes of subparagraph (A), the term ‘appli-
22 cable percentage’ means the percentage (not
23 greater than 25 percent) equal to the sum of—

24 “(i) 15 percent, plus

1 “(ii) 1 percentage point for each
2 whole dollar by which \$20 exceeds the ref-
3 erence price for crude oil for the calendar
4 year preceding the calendar year in which
5 the taxable year begins.

6 For purposes of this paragraph, the term ‘ref-
7 erence price’ means, with respect to any cal-
8 endar year, the reference price determined for
9 such calendar year under section 29(d)(2)(C).

10 “(C) MARGINAL PRODUCTION.—The term
11 ‘marginal production’ means domestic crude oil
12 or domestic natural gas which is produced dur-
13 ing any taxable year from a property which—

14 “(i) is a stripper well property for the
15 calendar year in which the taxable year be-
16 gins, or

17 “(ii) is a property substantially all of
18 the production of which during such cal-
19 endar year is heavy oil.

20 “(D) STRIPPER WELL PROPERTY.—For
21 purposes of this paragraph, the term ‘stripper
22 well property’ means, with respect to any cal-
23 endar year, any property with respect to which
24 the amount determined by dividing—

1 “(i) the average daily production of
2 domestic crude oil and domestic natural
3 gas from producing wells on such property
4 for such calendar year, by

5 “(ii) the number of such wells,
6 is 15-barrel equivalents or less.

7 “(E) HEAVY OIL.—For purposes of this
8 paragraph, the term ‘heavy oil’ means domestic
9 crude oil produced from any property if such
10 crude oil had a weighted average gravity of 20
11 degrees API or less (corrected to 60 degrees
12 Fahrenheit).”

13 (b) CONFORMING AMENDMENT.—Paragraph (3) of
14 section 613A(c) (defining depletable oil quantity) is
15 amended to read as follows:

16 “(3) DEPLETABLE OIL QUANTITY.—For pur-
17 poses of paragraph (1), the taxpayer’s depletable oil
18 quantity is 1,000 barrels.

19 (c) EFFECTIVE DATE.—The amendments made by
20 this section shall apply to taxable years beginning after
21 December 31, 1994.

22 **SEC. 203. ALLOCATION OF DEPLETABLE QUANTITIES.**

23 (a) IN GENERAL.—Subparagraphs (A) and (B) of
24 section 613A(c)(7) (relating to special rules for production
25 in excess of depletable quantities) are each amended by

1 inserting “of such quantity allocated to the property by
 2 the taxpayer, or, if the taxpayer elects not to make the
 3 allocation, that amount” after “shall be that amount”.

4 (b) EFFECTIVE DATE.—The amendments made by
 5 this section shall apply to taxable years beginning after
 6 December 31, 1994.

7 **SEC. 204. PERCENTAGE DEPLETION RATE FOR MARGINAL**
 8 **PRODUCTION.**

9 (a) IN GENERAL.—Subparagraph (B) of section
 10 613A(c)(6), as amended by section 202(a), is amended to
 11 read as follows:

12 “(B) APPLICABLE PERCENTAGE.—For
 13 purposes of this paragraph, the term ‘applicable
 14 percentage’ means the percentage (not greater
 15 than 25 percent) equal to the sum of—

16 “(i) 15 percent, plus

17 “(ii) 1 percentage point for each
 18 whole dollar by which \$20 exceeds the ref-
 19 erence price for crude oil for calendar year
 20 1994 (determined under section
 21 29(d)(2)(C)).”

22 (b) EFFECTIVE DATE.—The amendments made by
 23 this section shall apply to taxable years beginning after
 24 December 31, 1994.

1 **TITLE III—OTHER PROVISIONS**

2 **SEC. 301. ELECTION TO EXPENSE GEOLOGICAL AND GEO-**
3 **PHYSICAL EXPENDITURES.**

4 (a) IN GENERAL.—Section 263 (relating to capital
5 expenditures) is amended by adding at the end the follow-
6 ing new subsection:

7 “(j) GEOLOGICAL AND GEOPHYSICAL EXPENDI-
8 TURES FOR DOMESTIC OIL AND GAS WELLS.—Notwith-
9 standing subsection (a), a taxpayer may elect to treat geo-
10 logical and geophysical expenses incurred in connection
11 with the exploration for, or development of, oil or gas with-
12 in the United States (as defined in section 638) as ex-
13 penses which are not chargeable to capital account. Any
14 expenses so treated shall be allowed as a deduction in the
15 taxable year in which paid or incurred.”

16 (b) CONFORMING AMENDMENT.—Section 263A(c)(3)
17 is amended by inserting “263(j),” after “263(i),”.

18 (c) EFFECTIVE DATE.—

19 (1) IN GENERAL.—The amendments made by
20 this section shall apply to expenses paid or incurred
21 after the date of the enactment of this Act.

22 (2) TRANSITION RULE.—In the case of any ex-
23 penses described in section 263(j) of the Internal
24 Revenue Code of 1986 which were paid or incurred
25 on or before the date of the enactment of this Act,

1 the taxpayer may elect, at such time and in such
2 manner as the Secretary of the Treasury may pre-
3 scribe, to amortize the unamortized portion of such
4 expenses over the 36-month period beginning with
5 the month in which the date of the enactment of this
6 Act occurs. For purposes of this paragraph, the
7 unamortized portion of any expense is the amount
8 remaining unamortized as of the first day of the 36-
9 month period.

10 **SEC. 302. ENHANCED OIL RECOVERY CREDIT.**

11 (a) EXPANSION OF PROJECTS ELIGIBLE FOR CRED-
12 IT.—

13 (1) IN GENERAL.—Clause (i) of section
14 43(c)(2)(A) (defining qualified enhanced oil recovery
15 project) is amended to read as follows:

16 “(i) which involves the application (in
17 accordance with sound engineering prin-
18 ciples) of 1 or more secondary or tertiary
19 recovery methods which can reasonably be
20 expected to result in more than an insig-
21 nificant increase in the amount of crude oil
22 or natural gas which ultimately will be re-
23 covered,”.

24 (2) CONFORMING AMENDMENTS.—

1 (A) Subparagraph (C) of section 43(c)(1)
2 is amended to read as follows:

3 “(C) Any cost paid or incurred (whether or
4 not chargeable to capital account) for any
5 injectant or other costs which are used as part
6 of a qualified enhanced oil recovery project,
7 other than a recoverable hydrocarbon injectant
8 described in section 193(b)(2).”

9 (B) Section 43(c)(4) is amended to read as
10 follows:

11 “(4) SECONDARY AND TERTIARY RECOVERY
12 METHODS.—For purposes of paragraph (2), second-
13 ary and tertiary recovery methods shall include—

14 “(A) tertiary recovery methods described
15 in section 193(b)(3),

16 “(B) immiscible nonhydrocarbon gas dis-
17 placement, and

18 “(C) other secondary and tertiary recovery
19 methods certified in accordance with paragraph
20 (2)(B).”

21 (b) CREDIT ALLOWABLE AGAINST MINIMUM TAX.—

22 (1) IN GENERAL.—Subsection (c) of section 38
23 (relating to limitation based on amount of tax), as
24 amended by section 101(c), is amended by redesign-
25 ating paragraph (4) as paragraph (5) and by in-

1 serting after paragraph (3) the following new para-
2 graph:

3 “(4) SPECIAL RULES FOR ENHANCED OIL RE-
4 COVERY CREDIT.—

5 “(A) IN GENERAL.—In the case of the en-
6 hanced oil recovery credit—

7 “(i) this section and section 39 shall
8 be applied separately with respect to the
9 credit, and

10 “(ii) in applying paragraph (1) to the
11 credit—

12 “(I) subparagraph (A) shall not
13 apply, and

14 “(II) the limitation under para-
15 graph (1) (as modified by subclause
16 (I)) shall be reduced by the credit al-
17 lowed under subsection (a) for the
18 taxable year (other than the enhanced
19 oil recovery credit).

20 “(B) ENHANCED OIL RECOVERY CRED-
21 IT.—For purposes of this subsection, the term
22 ‘enhanced oil recovery credit’ means the credit
23 allowable under subsection (a) by reason of sec-
24 tion 43(a).”

25 (2) CONFORMING AMENDMENTS.—

1 (A) Subclause (II) of section
 2 38(c)(2)(A)(ii), as amended by section 101(c),
 3 is amended by striking “or the oil and gas pro-
 4 duction credit” and inserting “, the oil and gas
 5 production credit, or the enhanced oil recovery
 6 credit”.

7 (B) Subclause (II) of section
 8 38(c)(3)(A)(ii) is amended by inserting “or the
 9 enhanced oil recovery credit” after “production
 10 credit”.

11 (c) EFFECTIVE DATE.—The amendments made by
 12 this section shall apply to taxable years beginning after
 13 December 31, 1994.

14 **SEC. 303. ELECTION FOR OPTIONAL 5-YEAR WRITEOFF OF**
 15 **INTANGIBLE DRILLING COSTS.**

16 (a) OPTIONAL ELECTION FOR MINIMUM TAX PUR-
 17 POSES.—

18 (1) IN GENERAL.—Section 56(a) is amended by
 19 adding at the end the following new paragraph:

20 “(9) INTANGIBLE DRILLING COSTS.—If the tax-
 21 payer elects to have this paragraph apply, the tax-
 22 payer may disregard, for purposes of computing the
 23 taxpayer’s alternative minimum taxable income, an
 24 election under section 59(e) with respect to any por-

1 tion of any qualified expenditure described in section
2 59(e)(2)(C).”

3 (2) CONFORMING AMENDMENT.—Section 59(e)
4 is amended by adding at the end the following new
5 paragraph:

6 “(7) EXCEPTION FOR INTANGIBLE DRILLING
7 COSTS.—

**“For election not to have this subsection apply in
computing alternative minimum taxable income, see
section 56(a)(9).”**

8 (b) TIME FOR MAKING ELECTIONS.—Subparagraph
9 (B) of section 59(e)(4) is amended to read as follows:

10 “(B) TIME FOR MAKING ELECTION.—

11 “(i) IN GENERAL.—An election under
12 this subsection may be made or revoked at
13 any time before the period for filing a
14 claim for credit or refund (determined
15 after any extension) expires.

16 “(ii) PERIOD OF LIMITATION FOR AS-
17 SESSMENT.—The period for assessing a
18 deficiency attributable to any election
19 under clause (i) (or any revocation thereof)
20 shall not expire before the date 1 year
21 after the date the Secretary is notified of
22 the election (or revocation).”

23 (c) EFFECT OF ELECTION.—Paragraph (6) of section
24 59(e) is amended by adding at the end the following: “Any

1 deductions with respect to such portion shall not be treat-
2 ed as directly attributable to oil and gas properties for
3 purposes of section 57(a)(2)(C).”

4 (d) EFFECTIVE DATE.—The amendments made by
5 this section shall apply to taxable years beginning after
6 December 31, 1994.

7 **SEC. 304. ALLOCATION OF DEDUCTIONS IN DETERMINING**
8 **NET INCOME.**

9 (a) IN GENERAL.—Clause (ii) of section 57(a)(2)(C)
10 is amended by striking “allocable” and inserting “directly
11 attributable”.

12 (b) EFFECTIVE DATE.—The amendments made by
13 this section shall apply to taxable years beginning after
14 December 31, 1994.

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